



## **CITY MANAGER'S 6-POINT PLAN OF ACTION**

### **Points 2 and 4: In-Lieu Fees/Inter-Fund Transfers**

**CITY OF SUNNYVALE  
OFFICE OF THE CITY MANAGER**

**Interoffice Memorandum**

**TO:** The Honorable Mayor and City Council Members

**FROM:** Robert S. LaSala, City Manager

**SUBJECT:** Rental Rates and In-Lieu Fees/Inter-Fund Transfer Report

**DATE:** March 20, 2003

**COPIES:** ELT Members

I am enclosing a copy of the report describing changes to rental rates and in-lieu fees/inter-fund transfers. As you know, this report has been developed in response to the City's financial and budget crisis.

This report will be presented as part of the City Council's regular meeting on Tuesday, March 25, 2003 in Council Chambers. City staff will present report highlights, and will be available to answer questions or respond to comments. The report will be listed on the agenda as a public hearing item, which will allow the public will be able to provide comments, ideas, and opinions. As you will see, there is no recommendation included in the report. I will provide recommendations regarding modifications to services and/or levels of services that are associated with rental rates and in-lieu fees/inter-fund transfers as part of the overall service reduction presentation scheduled in April.

Please let me know if you have any questions or need additional information prior to the March 25<sup>th</sup> meeting.

## **Executive Summary**

This is the second in a series of planned special reports that are being prepared on one or more of the specific budget strategies described in the City Manager's 6-Point Plan of Action to the City's budget crisis. This report addresses rental rates and in-lieu fees/inter-fund transfers.

City staff annually updates rental rates and in-lieu fees/inter-fund transfers in the preparation of the City Manager's recommended budget and 10-year resource allocation plan (RAP). These updates are largely administrative activities to keep rental rates and in-lieu fees/inter-fund transfers current. The City Council adopts the updated rental rates and in-lieu fees/inter-fund transfers when it approves the budget and RAP.

This year, staff completed a more in-depth look at rental fees and in-lieu fees/inter-fund transfers with the intent to find approaches that could be appropriately used to recover expenses funded by the City's General Fund from other City funds. This report describes the initial results from these analyses, and changes that will be made to rental rates and in-lieu fees/inter-fund transfer schedules. These changes will contribute about \$xx annually (in equipment replacement costs only) to help close the \$11 million annual, structural gap between expenses and revenues in the General Fund.

## **Background**

### **I. Overview of Rental Rates, In-Lieu Fees/Inter-Fund Transfers**

The City of Sunnyvale is faced with an unprecedented financial and budget crisis. On January 28, 2003, the City Manager presented to the City Council a 6-Point Plan of Action to address this crisis. This report explained the basis of an \$11 million annual gap between expenses and revenues in the City's General Fund for FY 2003/2004 and beyond. This figure could increase if proposed state cutbacks in vehicle license fee revenues forwarded to California cities and counties are reduced.

This \$11 million gap represents an annualized, structural shortfall between revenues and expenses in the General Fund that will require a reduction in the size of city government in Sunnyvale. The January 28<sup>th</sup> report also defined six budget strategies that staff are presuming in order to close the \$11 million gap.

Two budget strategies called for staff to re-examine the existing formulas and schedules used to establish rental rates, and in-lieu fees/ inter-fund transfers. Both mechanisms are used in preparing the recommended City budget and Ten-Year Resource Allocation Plan (RAP). In general, rental rates can be considered as overhead charges to allocate the costs of support services such as vehicles and equipment, City office space and furniture, and communications and information technology equipment costs to operating programs. Rental rate expenses are assessed to operating programs based on the amount of building space occupied, the equipment in place, and/or the level of usage of the equipment.

In-lieu fees/inter-fund transfers are used to allocate designated City expenses to various funds that make up the City's budget and RAP. It is important to remember that there are many funds that make up the City's budget and RAP. State law allows (and sound financial practices require) that the costs of designated administrative services be allocated to the General Fund and other City funds. These allocations or in-lieu fees allow the costs for certain administrative services to be shared by all City funds. Inter-fund transfers are used to allocate the costs for these administrative services from the General Fund to other funds. For example, a portion of costs for financial management, human resource management and overall city management services is paid for by the City's enterprise funds. The General Fund pays for the balance of these costs.

## II. Types of Rental Rates

Rental rates include two key components: equipment costs and operating costs (i.e. personnel, materials, consumables, and other types of operating expenses). General Fund rental rates are used to allocate the costs of four types of support services to operating programs:

- Fleet Services: this rental rate reflects the cost of ownership of the City's fleet and equipment. This includes all rolling stock such as police cars, light and heavy-duty trucks, and backhoes or other specialized equipment. Fleet services also buys, repairs, and maintains a wide variety of equipment used by City staff in providing services. Currently, there are 371 vehicles and 262 pieces of equipment included in the fleet.
- Building Services: this rental rate reflects the cost of maintaining facilities, free standing furniture, modular furniture, and building equipment. Facilities Management maintains 91 buildings within the City including 38 public buildings, 48 buildings located within the Parks, 4 Community Center buildings, and a portion of the Water Pollution Control Plant. Facilities Management also purchases, repairs, and maintains equipment in these facilities ranging from HVAC systems to electrical, carpet, window coverings, appliances, and furniture.
- Technology Services: this rental rate reflects the costs of ownership of the City's computer system. Eight factors contribute to the total cost of this rental rate. They are: central computer maintenance, desktop computer maintenance, software maintenance, training, development of equipment specifications and/or applications, project maintenance, administrative and support services, and equipment replacement costs.
- Communication Services: this rental rate reflects the costs of ownership of the City's communication and information office equipment. Five equipment categories contribute to the total cost of this rental rate. They are: communication equipment, office equipment, mail services, print shop services, and telecommunication franchise (all KSUN related equipment).

Rental rates for fleet services are directly tied to the size of the City's workforce, especially the number of field services employees and public safety officials. Reductions in the workforce will result in fewer vehicles and equipment. This results in reductions to rental rates for fleet services.

Rental rates for building services, technology services, and communication services are tied less directly to the size of the workforce. For example, buildings, computer networks, and telephone systems will need to be maintained even if the workforce is reduced. When the size of workforce reductions results in closing a building, dropping a complete computer network, or eliminating a complete feature on a telephone system, these rental rates will see reductions attributable to a smaller workforce.

The costs for these services are recovered through rental rates that are charged to the operating budgets of various programs. The rental rates include both the direct costs for providing these services and the replacement costs for equipment. This assures that funds will be available to replace equipment at the most cost-effective times.

Several other types of specialized rental rates have been established to provide for the equipment replacement of designated programs, such as police services, recreation services, or the Wastewater program. Only the four rental rates listed above are allocated on a citywide basis.

### III. In-Lieu Fees/ Inter-Fund Transfers

The City's In-Lieu allocation process allocates administrative services incurred by the General Fund to enterprise and grant funds that use these services. Allocated expenses from non-General Fund funds are returned to the General Fund through inter-fund transfers. This allows for other City funds to help share the costs of these services.

The administrative costs that are currently allocated under this method include the General Fund programs of the Finance and Human Resources Departments, and the Offices of the City Manager and the City Attorney. The Utility Business Management program of the Finance Department is charged completely to the City's three utility enterprises. About xx% of the total annual costs for the remaining administrative services are allocated to the Water, Solid Waste, Wastewater, Community Recreation, and SCI3-Patent Library Funds. Roughly \$xx is returned annually to the General Fund through inter-fund transfers from these five funds.

### IV. Services and Levels of Services

The changes to rental rates and in-lieu fees/ inter-fund transfers described later in this report are presented to the City Council for its information only. No preliminary policy direction is required at this point in time. These changes will result in savings or funds which will be used to help close the \$11 million gap between expenses and revenues in the General Fund. In some cases, these changes will affect levels of service for certain City programs. These changes to levels of service will be described in this report, and presented to Council at this time for information only. Council will be asked to provide

preliminary policy direction in April on reductions to services and levels of service. Staff believes that it is Council's preference to consider reductions to services levels generated by changes to rental rates and in-lieu fees/inter-fund transfers when it considers all recommended changes to services and levels of service.

### **Key Findings**

#### **I. Overall Financial Effect of Changes to Rental Rates, and In-Lieu Fees/ Inter-Fund Charges**

Staff's re-examination of the formulas and schedules used in developing rental rates, and in-lieu fees/inter-fund transfers, has produced several key findings. These key findings translate into projected savings to the General Fund, beginning in FY 2003/2004. These savings represent both reduced costs for vehicles and equipment, and reduced operating costs. As indicated earlier, some of these savings will result in service level changes. These changes will be presented to Council to consider in providing preliminary policy direction in April. It should also be noted that these represent projected future savings; staff is continuing to analyze rental rates and in-lieu fees/inter-fund transfers. Final rates and fees will be included in the City Manager's recommended FY 2003/2004 budget.

The following summarizes the estimated savings generated by revisions to rental rates, and in-lieu fees/inter-fund transfers:

#### **Rental Rates**

- Fleet Services**

Equipment Schedule Adjustment	\$400,000 - \$500,000
Operating Reduction	\$150,000 - \$240,000
Total:	\$550,000 - \$740,000

- Building Services**

Equipment Schedule Adjustment	\$70,000
Operating Reduction	\$400,000
Total:	\$470,000

It should be noted that \$100,000 in savings in the equipment schedule adjustment had previously been identified, and used to fund wage increases for Sunnyvale Employee Association (SEA) employees, beginning in FY 2002 and continuing for the 20-year planning period.

- Technology and Communication Services

Equipment Schedule Adjustment	\$200,000
Operating Reduction	\$600,000
Total:	\$750,000

It should be noted that \$200,000 in savings in the equipment schedule adjustment had previously been identified, and used to fund wage increases for Sunnyvale Employee Association (SEA) employees, beginning in FY 2002 and continuing for the 20-year planning period.

#### In-lieu Fees/Inter-Fund Transfers

The estimated savings total \$xx. About 75-80% of these savings can be applied to the General Fund. The balance would be allocated to other funds. On a levelized basis, this would contribute \$xx annually in reducing the \$11 million gap between expenses and revenues in the General Fund.

#### II. Rental Rates: Key Findings

Staff analyzed existing rental rates for fleet, building, technology, and communication services by re-examining the assumptions, formulas, and schedules used to preparing the rental rates. This analysis generated several key findings. For example, staff looked at fleet services rental rates to see if extending the useful lives of vehicles and equipment would produce sufficient short term savings, without creating life/safety issues or significantly increasing maintenance costs in the long-term.

Public Works staff completed the fleet service analysis. This assessment concluded that a reduction in the size of the fleet, rather than extending the useful lives of vehicles and equipment, is the best approach to reduce rental rates. This approach will reduce rates without creating life/safety problems or costly, long-term maintenance issues. Future, planned workforce reductions also support the concept of a smaller fleet of vehicles and equipment. Reducing the size of the fleet would also result in:

- Maintaining the outcome measure for Fleet services program that establishes an average "uptime" or availability of vehicles and equipment at 98%;
- Significant reductions in the number of vehicles assigned to public safety personnel and public works employees as "take home" cars.

Changes to the City's practices regarding "take home" vehicles may require meet and confer sessions with employee associations. Human Resources staff is researching this issue, and will have information by the City Council's March 25<sup>th</sup> special meeting on rental rates and in-lieu fees/inter-fund transfers.

Staff projects that the size of the fleet will drop by 10-15%, in part because of service level reductions. The actual reductions to the fleet will be made to specific vehicle and

equipment classifications. Public Works staff are meeting with other departments to coordinate the reductions, and to identify any unforeseen effects of reducing the actual number of vehicles or equipment to specific department. Vehicles or equipment slated for reduction will be held for a limited time and used for necessary replacements. After this time period has elapsed, the vehicles or equipment will be sold at auction, surplus, or disposed of. Staff is also exploring shared use agreements with adjacent cities, school districts, and the county to jointly use certain types of specialized vehicles and equipment.

Parks and Recreation staff began its review of building rental rates along the same lines as facility services--could building maintenance and equipment replacement schedules be "stretched?" However, unlike the fleet service assessment, staff concluded that building maintenance and equipment schedules could be extended, resulting in significant cost savings without creating life/safety issues or significantly higher long-term maintenance costs.

Four components make up the building services rental rate. (It also should be noted that nearly 30% of this rental rate reflects the costs for electricity and water.) Several approaches will be used to generate savings, and reduce rental rates:

- Free standing furniture. Facilities Maintenance staff in the Parks and Recreation Department will implement a new practice for purchasing and maintaining office furniture. In the past, office furniture was replaced according to a pre-determined replacement schedule. Now, furniture replacement will be coordinated and managed by Facility Maintenance staff. Furniture requested to be replaced will be evaluated by Facility Maintenance staff. This evaluation will determine whether the furniture can be repaired or renovated, and continued to be used, rather than replaced. This new practice is projected to generate \$1 million in savings over a 20-year period in replacing furniture.
- Modular Furniture. As part of previous space planning efforts, the City established guidelines for the size of offices, meeting rooms, lobbies, and storage areas within City buildings. These guidelines also established that modular furniture would be used wherever possible in offices. The City has been purchasing high quality, used furniture in quantity for its future replacement needs. In addition, staff has purchased rolls of fabric at reduced costs to repair modular furniture when damaged, or to renovate modular furniture that show signs of wear. These strategies are projected to generate nearly \$600,000 in savings during the next 20 years.
- Building Equipment. Many types of equipment and furnishings are purchased, repaired, and maintained by Facilities Management staff, such as carpets, blinds, small appliances, and room-sized HVAC systems. Staff analyzed existing replacement schedules, and determined where these schedules could be reasonably extended without compromising safety or long-term maintenance expenses. The extended schedules are expected to generate nearly \$1.4 million in savings during the next 20 years.
- Minor Equipment. A similar approach was used for the purchase, repair, and maintenance of equipment valued at \$1,000 or lower. Examples of these types of



equipment include xx get from Larry. Extending the useful lives for this type of equipment is projected to generate \$375,000 in savings during the next 20 years.

The combined savings in building services rental rates total about \$3.4 million during the next 20 years. This equates to about \$170,000 in savings annually. It should be noted that about \$100,000 of these savings was previously committed to fund the SEA wage increases for the next 20 years.

Information Technology Department staff completed the rental rate re-examination of technology and communication services. They also conducted the review along the same lines as facility services--could computer hardware and software, and communication equipment schedules be "stretched?" They concluded that schedules could be stretched, resulting in significant cost savings without creating life/safety issues or significantly higher long-term maintenance costs.

Three broad components make up the technology and communication services rental rates. Several approaches will be used to generate savings, and reduce rental rates:

Communication and Office Equipment. This rental rate covers various types of communication equipment such as telephones, telephone system equipment, and radios. Staff determined that the useful life for this equipment could be extended from its existing 15 year to 20 years. For example, the Public Safety radio system was purchased and installed in 1975, and replaced in 1999. Extending the useful lives for this type of equipment is projected to generate nearly \$60,000 annually in savings during the next 20 years.

Computer Hardware. This rental rate covers various types of computer hardware such as workstations, laptops, and file servers. Staff determined that the useful life for this equipment could be extended. For example, laptops can be extended from the existing three years to five years; file servers can be extended from five years to 10 years. **Insert example** Extending the useful lives for this type of computer hardware is projected to generate nearly \$100,000 annually in savings during the next 20 years.

Computer Software. This rental rate covers various types of computer software, especially major applications such as payroll and financial management systems. Staff determined that the useful life for this equipment could be extended from its existing 10 years to 15 years. For example, both the payroll system used by the Finance Department and the circulation system used in the Library are being currently replaced. The payroll system went on line in 1987, and the Library system in 1985. Extending the useful lives for this type of computer software is projected to generate nearly \$13,000 annually in savings during the next 20 years.

Together, these projected savings in rental rates total more than \$170,000 annually.

### III. In Lieu Fees/Inter-Fund Transfers

Finance staff reviewed the current practices used in developing in-lieu fees/inter-fund transfer schedules to the General Fund. There are many assumptions built into the formulas that produce the annual in-lieu fees and transfers between funds. The formulas and assumptions have been in place for many years. Staff's initial examination produced two key findings. First, because of the complexity of existing in-lieu fees/inter-fund transfer, a thorough, detailed examination of the assumptions and current schedules should be completed before any wholesale changes are made to the process. This in-depth analysis can be completed during FY 2003/2004.

Second, the initial study did identify some minor modifications that could be implemented now without jeopardizing the in-depth analysis. These minor changes could produce some appropriate reallocation of General Fund expenses to other funds. For example:

Cashiering services. The Finance Department's Treasury Division provides cashiering services for various activities paid for through the General Fund and other funds. Currently, a portion of the cost of cashiering services is paid for by the General Fund, with the remaining paid by various utility funds. Staff is currently reviewing the cashiering activity, and will make adjustments to the cashiering in-lieu fees as appropriate to reflect the full cost of providing cashiering services for utility funds. These changes will be included in the recommended FY 2003/2004 budget.

Financial Auditing. The City contracts with an independent auditor to conduct an audit of the City's financial statements. This auditor's opinion on the financial statements are reflected in the City's Comprehensive Annual Financial Report. The audit includes the Utility Enterprise Funds. Currently, audit expenses are paid for through the General Fund. Allocating a portion of these costs to the Utility Enterprise Funds would result in about \$23,000 savings annually to the General Fund.

Bill Printing and Mailing Services. As part of the overall print shop services, the Information Technology Department provides bill printing, mail delivery, and mail pick up services for utility billing activities. Staff is reviewing the time and materials required to perform these functions. Allocating a portion of these costs, which are currently paid for through the General Fund, to other City funds, will result in about \$32,000 in savings annually to the General Fund.

Finally, staff is exploring the feasibility of developing a new in-lieu fee from the Solid Waste Management Fund to the General Fund for use of the property where the SMaRT Station is located. The 9.5 acre site is owned by the City. An inter-fund transfer would be used to move funds from the Solid Waste Management Fund to the General Fund to pay annual rent for using this property. This annual rental fee could generate a new revenue stream to the General Fund in an amount ranging from \$232,000 per year. Additional staff work will be required to fully explore this idea.

The combined projected savings in in-lieu fees/inter-fund transfers total more than \$55,000 annually.

## **Next Steps**

### **I. Projected Annual Savings**

The re-examination of rental fees and in-lieu fees/inter-fund transfers has resulted in several changes to existing practices, formulas, and schedules. These changes will result in a total of \$xx annually in projected savings, as shown:

#### **Rental Rates**

• Fleet Services:	\$400 - \$500,00
• Building Services:	\$70,000
• Communications and Office Equipment:	\$200,000
 Total:	 \$670,000 - \$770,000

In-Lieu Fees/ Inter-Fund Transfers:	\$55,000
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This combined \$xx projected savings represents equipment replacement costs only. An additional \$xx in projected operating cost savings could also be realized, depending on the City Manager's recommendations regarding Fleet, Building, and Information Technology services, and final City Council approval. The \$11 million gap between expenses and revenues in the General Fund could be reduced by \$xx by changes to rental fees and in-lieu fees/inter-fund transfers. This figure would increase when operating cost reductions are included.

### **II. Opportunities for Public Education and Comment**

City staff will present the changes to rental rates and in-lieu fees/inter-fund transfers to the City Council on Tuesday, March 25, 2003, at a special Council meeting beginning at 6:30 p.m. No preliminary policy direction will be required at this meeting. Council will accept these changes when it adopts the final budget for FY 2003/2004 and Resource Allocation Plan in June.

The public will have an opportunity to comment on the changes at the March 25<sup>th</sup> meeting. In addition, two community budget meetings have been scheduled to inform the public about rental rates and in-lieu fees/inter-fund transfers, and to present the changes. They are:

- April 15, 2003, at the Sunnyvale Public Library Program Room, at 10:00 am.
- April 16, 2003, at Cherry Chase Elementary Room, at 7:00 pm.

Both meetings will be held prior to Council's final action on the budget in June.